INDEX

	Page
Opinions below	1
Jurisdiction	1
Question presented	2
Statutes involved	2
Statement	3
Argument	4
Conclusion	9

CITATIONS

Cases:	
Black v. *Commissioner*, 114 F. 2d 355	7, 8
Burnet v. *Leininger*, 285 U. S. 136	5, 6
Commissioner v. *Tower*, 327 U. S. 280	7
Larsen v. *Burnet*, 50 F. 2d 308	5
Lusthaus v. *Commissioner*, 327 U. S. 293	7
Statutes:	
Internal Revenue Code:	
Sec. 181 (26 U. S. C. 1940 ed., Sec. 181)	2, 4
Sec. 182 (26 U. S. C. 1940 ed., Sec. 182)	2, 5
Revenue Act of 1938, c. 289, 52 Stat. 447:	
Sec. 181	2
Sec. 182	2

In the Supreme Court of the United States

OCTOBER TERM, 1946

No. 950

GRANVILLE C. MORTON, PETITIONER

v.

KATE THOMAS, AS COMMUNITY SURVIVOR OF THE ESTATE OF W. A. THOMAS, DECEASED, FORMER COLLECTOR OF INTERNAL REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The opinion of the District Court (R. 46–47) is not reported. The opinion of the Circuit Court of Appeals (R. 53–56) has not yet been reported.

JURISDICTION

The judgment of the Circuit Court of Appeals was entered on December 6, 1946. (R. 56.) A petition for rehearing (R. 57–61) filed on December 21, 1946 (R. 57), was denied on January 7, 1947 (R. 62). The petition for a writ of certiorari was filed on January 24, 1947. The juris-

diction of this Court rests on Section 240 (a) of the Judicial Code, as amended by the Act of February 13, 1925.

QUESTION PRESENTED

Whether the court below correctly held that the taxpayer's distributive share of partnership earnings was taxable to him and that his daughter was not shown to have such an interest therein that any portion of that income could be attributable to her for tax purposes.

STATUTES INVOLVED

Internal Revenue Code:

> SEC. 181. PARTNERSHIP NOT TAXABLE.
>
> Individuals carrying on business in partnership shall be liable for income tax only in their individual capacity.
>
> (26 U. S. C. 1940 ed., Sec. 181.)
>
> SEC. 182. TAX OF PARTNERS.
>
> In computing the net income of each partner, he shall include, whether or not distribution is made to him—
>
> * * * * *
>
> (c) His distributive share of the ordinary net income or the ordinary net loss of the partnership, computed as provided in section 183 (b).
>
> (26 U. S. C. 1940 ed., Sec. 182.)

The provisions of Sections 181 and 182 (c) of the Revenue Act of 1938, c. 289, 52 Stat. 447, are identical with the corresponding provisions of the Internal Revenue Code quoted above.

STATEMENT

This suit was brought for the refund of a portion of income taxes paid for the years 1938 through 1941, the taxpayer claiming that one-half of the income he had reported as derived from a partnership was not taxable to him but should have been taxed to his daughter. (R. 2, 5–6.) The taxpayer resides and has his place of business in Dallas, Texas. (R. 1–2, 30.)

The taxpayer was the only witness and his testimony was to the following effect (R. 32–42): In 1932 he established a business known as the Morton Potato Chip Company. This was done with community property and community efforts. In 1937 L. M. Mitchell was admitted into the business, he and the taxpayer being associated as partners, and the profits being shared on the basis of 40 percent to Mitchell and 60 percent to the taxpayer. (R. 54.)

In 1938 the taxpayer's wife died. At that time their share of the partnership assets was worth approximately $27,000; at the time of the trial of this case the assets of the business were greatly enhanced in value. Prior to the time that his wife died, the taxpayer's share of the earnings from the business was considered as community property and he and his wife paid their federal income taxes on that basis. (R. 54.)

After the death of his wife and until 1944, the partnership continued without change and the

taxpayer, both on the partnership books and in his income tax returns, treated 60 percent of the income from the partnership as his own. In 1944, after having been advised by a tax expert, the taxpayer started making tax returns on the basis that only 30 percent of the partnership income was taxable to him and that 30 percent was taxable to his daughter. He also filed, on January 19, 1944, claims for refund of part of the taxes paid for the period 1938 through 1941 on the ground that a one-half interest in the partnership assets and profits devolved upon his daughter at the death of his wife. (R. 7–28, 54.) These claims were rejected on October 5, 1945 (R. 29), and the taxpayer then filed this suit to recover the amounts allegedly overpaid. The District Court entered judgment against the taxpayer (R. 48–49) and, on appeal, the judgment was affirmed by the Circuit Court of Appeals (R. 56). Because it decided that the taxpayer had not made any overpayment, the court below did not pass on the holding of the District Court (R. 46) that the claims for refund for 1938 and 1939 were in any event barred by Section 322 of the Internal Revenue Code.

ARGUMENT

1. The decision of the Circuit Court of Appeals is correct.

Under Section 181 of the Internal Revenue Code, *supra*, individuals carrying on business in

partnerships are made liable for income tax in their individual capacity, and under Section 182 (c), *supra*, each partner is required to include in the computation of his net income his distributive share of the ordinary net income of the partnership whether or not distribution is made to him.

The court below has properly observed (R. 55) that no valid contention has been or could be made that the taxpayer's daughter was a partner in the partnership business carried on by the taxpayer and Mitchell, for there is no testimony whatsoever that she ever agreed, or that anybody agreed for her, to act as, or be, a partner. The determination of the District Court (R. 47) that the only partners were the taxpayer and Mitchell was therefore correctly affirmed by the court below. Under the plain language of the statute the entire income of the partnership is taxable to these two partners, and the taxpayer accordingly correctly returned his 60 percent distributive share as his income in the taxable years here involved. *Burnet* v. *Leininger*, 285 U. S. 136; *Larsen* v. *Burnet*, 50 F. 2d 308 (App. D. C.).

The taxpayer contends, however (Br. 6), that his daughter had, upon the death of her mother in 1938, succeeded by operation of law to absolute ownership of the corpus of one-half of his partnership interest and under the local law of Texas was the actual beneficial owner of one-half of the taxpayer's distributive share of the partnership's

income and hence that the taxpayer was not taxable on this portion of the income. A similar contention was rejected by this Court in *Burnet* v. *Leininger, supra,* where this Court said (p. 141):

> The respondent urges that the assignment to his wife was of one-half of the *"corpus"* of his interest and that this *"corpus"* produced the income in question. The characterization does not aid the contention. That which produced the income was not Mr. Leininger's individual interest in the firm, but the firm enterprise itself, that is, the capital of the firm and the labor and skill of its members employed in combination through the partnership relation in the conduct of the partnership business. There was no transfer of the *corpus* of the partnership property to a new firm with a consequent readjustment of rights in that property and management. If it be assumed that Mrs. Leininger became the beneficial owner of one-half of the income which her husband received from the firm enterprise, it is still true that he, and not she, was the member of the firm and that she had only a derivative interest.
>
> The statute dealt explicitly with the liability of partners as such. [Referring to Section 218 (a) of the Revenue Acts of 1918, c. 18, 40 Stat. 1057, and 1921, c. 136, 42 Stat. 227, now Section 181 of the Internal Revenue Code.] Applying to this case, the statute provided that there should be included in computing the net income of

> Leininger his distributive share of the net income of the partnership. That distributive share, as he himself stated in his return on behalf of the partnership, was one-half. In view of the clear provision of the statute, it cannot be said that Leininger was required to pay tax upon only a part of this distributive share because of the assignment to his wife. * * *

See also *Commissioner* v. *Tower,* 327 U. S. 280; *Lusthaus* v. *Commissioner,* 327 U. S. 293.

Under the record in the present case, as made, no question is presented with respect to the right of the taxpayer to an offsetting deduction because of any liability of either himself or of the partnership to the taxpayer's daughter because of the use in the partnership business of any property of hers, nor is the amount of any such supposed liability shown by the record. The court below accordingly properly held (R. 54–55) that these questions are without bearing on the determination of the question involved.

2. *Black* v. *Commissioner,* 114 F. 2d 355 (C. C. A. 9th), which the taxpayer relies on (Br. 7–9) is not in conflict with the decision below. The income there in question was derived from certain farm land in the State of Washington which the taxpayer and his brother had acquired from their parents. The taxpayer's share of such land was held by the court (p. 357) to be the community property of the taxpayer and his wife. The tax-

payer and his brother entered into a partnership to *operate* the land, the court pointing out (p. 358) that the partnership did not own the land. The court held (p. 359) that the portion of the income attributable to the community land itself to which the taxpayer's wife was entitled, was not taxable to her husband but that the portion of the partnership income attributable to the personal services of the taxpayer was taxable to him alone. In the present case, the taxpayer's daughter had no interest similar or analogous to the interest of the taxpayer's wife in the *Black* case. The partnership business involved here was completely different from a partnership to operate land, title and ownership of which was not in the partnership. Here the partnership owned the assets employed in the partnership business with, at most, a right on the part of the taxpayer's daughter to an accounting. For all that the record in the present case shows, the income of the partnership here involved may have been attributable primarily to the personal efforts and skill of the two partners, rather than to the capital employed in the partnership. There has been no effort on the part of the present taxpayer to establish what portion of the partnership's income was attributable to the capital employed by the partnership. Clearly the taxpayer's daughter was not entitled to a distributive share of the partnership's income as such, and accordingly there is no basis for a

contention that the taxpayer's distributive share should not be included in the computation of his net income as provided by the statute.

CONCLUSION

The decision below is correct. No conflict in decisions is presented. Accordingly, further review of the case would not be warranted, and the petition for a writ of certiorari should be denied.

Respectfully submitted.

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